(4)

No. 90-1029

In The

Supreme Court of the United States

October Term, 1990

EASTMAN KODAK COMPANY,

Petitioner,

vs.

IMAGE TECHNICAL SERVICE, INC., J-E-S-P CO., INC.; SHIELDS BUSINESS MACHINES, INC.; MICROGRAPHIC SERVICES, INC.; MICRO MAINTENANCE, INC.; ATLANTA GENERAL MICROFILM CO., INC.; ROGER KATONA, d/b/a G. & S. ELECTRONICS; AMTECH EQUIPMENT MAINTENANCE, INC.; ADVANCED SYSTEMS SERVICE, INC.; B.C.S. TECHNICAL SERVICES, INC.; BOB INGLE INC.; DATA PROX EQUIPMENT CO.; FISHER MICROGRAPHICS, INC.; I.O.A. DATA CORP.; SEARLE ENTERPRISES, INC., d/b/a MICRO IMAGE; MIDWEST MICROFILM EQUIPMENT & SERVICES, INC.; OMNI MICROGRAPHIC SERVICES INC.; AND CPO LTD.,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether it was error for the Court of Appeals to reverse a summary judgment, granted after minimal discovery, against plaintiff independent service organizations ("ISOs") on their *per se* claim under section 1 of the Sherman Act, where the limited record developed in the District Court, considered in the light most favorable to plaintiffs, showed that (a) the defendant manufacturer had tied the availability of repair parts for its photocopy and micrographic machines to the agreement of its customers not to purchase service from ISOs, (b) competition in the interbrand machine market had not prevented the manufacturer from successfully forcing its service on a large number of its customers, and (c) the manufacturer's service was in many cases not wanted by these customers, as evidenced by the fact that the manufacturer charged twice as much for service as did ISOs, its service was on occasion inferior to that offered by ISOs, and the manufacturer had on occasion reduced its service prices in response to competition from ISOs.

2. Whether it was error for the Court of Appeals to reverse a summary judgment, granted after minimal discovery, against plaintiff ISOs under section 2 of the Sherman Act, where the limited record developed in the District Court, considered in the light most favorable to plaintiffs, showed that (a) repair parts controlled by the defendant manufacturer are essential components for the repair of defendant's micrographic and photocopy machines, (b) the manufacturer's control over parts gives it monopoly power in the market for service of its machines, and (c) the manufacturer had changed its prior

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policy of selling parts to ISOs and had presented no legitimate business justifications for its change of policy.

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BRIEF IN OPPOSITION

STATEMENT OF THE CASE

A. The Parties and the Photocopy – Micrographic Service Market

This case concerns competition between petitioner Eastman Kodak Company ("Kodak"), one of the largest manufacturers of photocopy and micrographic machines, and the 18 respondent independent service organizations

("ISOs")[1], in the market for servicing Kodak photocopy and micrographic equipment.[2]

This service market is a large and lucrative one for Kodak, because the cost of service and supplies exceeds the cost of the equipment over its useful life. Kodak does not have a dominant share in either the market for photocopy or micrographic equipment, but Kodak acknowledged below that it does have about 23% of the market for high-volume photocopy machines, and somewhat less than 20% of the market for micrographic machines. Petitioner's Appendix ("Pet. App.") at 8A, n.3.

Until the early 1980s, Kodak had little competition for the servicing of its equipment. Beginning in the early 1980s, however, many ISOs were formed. *Id.* at 3A. These small businesses were able to become profitable and grow by offering service equal to or better than Kodak's, at a price substantially less than Kodak's.

Until 1985, the number of ISOs grew rapidly. *Id.* This was not surprising in view of the price and quality of service offered. In several cases, ISOs agreed to provide service to customers having a large number of Kodak machines at one-half the price quoted by Kodak. *Id.* at 10A. The quality of the service was also good, as evidenced by the fact that one ISO was asked to bid for additional State of California business after providing superior service under its initial contracts with the State.

In order to compete with Kodak, the ISOs found it necessary to buy and to maintain stocks of spare parts, which were available only from Kodak itself or from third-party manufacturers who made the parts pursuant to contracts with Kodak. *Id.* at 3A.

[1] The caption of the petition identifies all parties in the lower court. The 18 respondents have no corporate parents and no subsidiaries other than wholly-owned subsidiaries.

[2] Micrographic equipment is used to make, store, retrieve, read or print a micro image such as microfilm or microfiche.

Until 1985, Kodak imposed no restrictions on who could buy its micrographic parts (provided the customers were credit-worthy), nor did it discriminate among micrographic parts customers as to price or availability. In 1985, however, Kodak changed its policy. It announced that henceforth, it would not sell replacement parts to ISOs for its new micrographic products at all. *Id.* In 1986, Kodak announced that even as to "old" micrographic equipment, it would sell parts only to established ISO customers, such orders would not be filled as promptly as before, certain classes of parts that rarely broke down would no longer be sold to ISOs, and the previous discount for non-rush orders would be eliminated. ISOs who serviced Kodak photocopy machines experienced a similar constriction of parts availability.[3]

In late 1986, Kodak formalized its change in parts policy by modifying its sales contracts with machine owners. The new agreement expressly provided that Kodak would sell replacement parts *only* to customers who serviced their own machines and did not use ISOs. In other words, by late 1986, Kodak formally conditioned the availability of repair parts on its customers' agreement *not* to purchase service from ISOs.

After unsuccessful attempts to negotiate with Kodak, the respondents filed the instant antitrust suit in April of 1987.

[3] Kodak claimed in the District Court that it has never knowingly sold photocopy replacement parts to ISOs since entering the photocopy business in 1975. Respondents dispute this, because at least some ISOs were able to purchase spare parts for copiers directly from Kodak without restrictions until Kodak began to lose significant service business to these ISOs. Pet. App. 13A-14A.

B. The Proceedings Below

1. The Summary Judgment in the District Court

Four months later, in August of 1987, before any discovery had been conducted, Kodak moved for summary judgment in the District Court. In response to Kodak's motion, the District Judge permitted the ISOs to propound one set of interrogatories and serve one request for production of documents on Kodak, as well as to take "no more than four depositions." Pet. App. 36B. The District Judge subsequently permitted the ISOs' counsel to take two additional depositions on the issue of market power, but no other discovery was permitted before Kodak's motion was ruled upon.[4] The ISOs' evidence on the summary judgment motion consisted mainly of declarations from ISO personnel detailing the facts set forth above. ISOs' counsel requested further discovery pursuant to F.R.C.P. 56(f), but this was denied.

On April 15, 1988, the District Court (without hearing oral argument) granted Kodak's summary judgment motion in its entirety. Despite the complaint's allegations that Kodak had tied its parts to service, the District Court found no tie-in under section 1 of the Sherman Act, 15 U.S.C. § 1:

> There is no evidence of any [tying] arrangement in this case. In selling its copiers and imaging equipment, Kodak does not require the buyer to agree to purchase parts or service from Kodak. Nor does it condition the sale of one product on the buyer's purchase of another product . . . A Kodak customer can buy equipment without having to buy parts; and he can buy part[s] if he simply owns Kodak equipment.

[4] Even this description of the limited discovery permitted is somewhat misleading, because Kodak objected to many of the ISOs' interrogatories and document requests. When the ISOs sought to move to compel responses, the District Judge refused to entertain the motion.

Pet. App. 32B-33B (citations omitted). The District Court treated Kodak's refusal to sell replacement parts to ISOs simply as an exercise of "the right of a manufacturer unilaterally to select its customers and to refuse to sell to others." *Id.* at 33B.

The District Judge was equally dismissive of the ISOs' monopolization and attempted monopolization claims under section 2 of the Sherman Act, 15 U.S.C. § 2:

> Plaintiffs contend that Kodak has a dominant share of a purported market for servicing Kodak copiers and micrographic equipment. Assuming without deciding that such a market can be found to exist and that Kodak has market power in it, plaintiffs have not come forward with any facts to suggest that Kodak has attempted to leverage power in that market to gain competitive advantage in another market.

Id. at 35B.

2. The Reversal of the Summary Judgment By The Ninth Circuit

On May 1, 1990, the Ninth Circuit, in a 2-1 decision, reversed the summary judgment granted by the District Court. After noting that a tie-in can exist not only where a seller conditions the availability of one product on the buyer's agreement to purchase a second, but also where the buyer "agrees that he will not purchase that [second] product from any other supplier," *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 5-6 (1958), the Ninth Circuit agreed with the respondents here that the District Court had misperceived the tie, because "Kodak has tied parts to service, not equipment to parts or parts to equipment." Pet. App. 4A-5A.

The Court of Appeals rejected Kodak's argument that, as a matter of law, parts and service could not comprise separate markets:

> Kodak's argument presents, at best, a disputed issue of fact. That products must be used

> together does not eliminate the possibility that they form distinct markets . . . Kodak's policy of allowing customers to purchase parts on condition that they agree to service their own machines suggests that the demand for parts can be separated from the demand for service. Kodak does not dispute appellants' claim that some equipment owners have (perhaps surreptitiously) bought service from ISOs and parts from Kodak. Nor does Kodak dispute appellants['] claim that other equipment owners would have contracted with ISOs for service if they could have obtained parts separately.

Pet. App. 6A-7A (citations omitted).

The Court of Appeals also rejected Kodak's argument that, as a matter of law, vigorous competition in the interbrand market for equipment meant that Kodak could not have sufficient economic power to force an illegal tie in the "aftermarket" for parts. Although acknowledging Kodak's point that competition in the equipment market might be shown to cause Kodak customers to switch to a different equipment brand if Kodak attempted to tie "supercompetitively priced service to parts," the Ninth Circuit concluded this issue could not be resolved on the record before it. Noting that the District Judge had "permitted only very limited discovery on the market power issue," *id.* at 10A, n.4, the Court of Appeals said:

> [W]e cannot uphold the district court's grant of summary judgment on this theoretical basis. Not only do we lack the benefit of the district court's consideration of the market power issue, we are presented with a record that was not fully developed through discovery on this issue. Furthermore, market imperfections can keep economic theories about how consumers will act from mirroring reality. *See Jefferson Parish*, 466 U.S. at 15 n.24 . . . (noting that market imperfections can keep consumers from seeing the price

> and quality implications of a tying arrangement). While appellants have not conducted a market analysis and pin-pointed specific imperfections in the copier and micrographic markets, a requirement that they do so in order to withstand summary judgment would elevate theory above reality. It is enough that appellants have presented evidence of actual events from which a reasonable trier of fact could conclude that Kodak has power in the interbrand market and that competition in the interbrand market does not, in reality, curb Kodak's power in the parts market.

Id. at 10A (citations and footnote omitted).

The Ninth Circuit closed its discussion of the tie-in issue by noting that as to the three business justifications[5] Kodak had offered for its parts policy – to insure the best service, reduce inventory costs and prevent free-riding by ISOs on Kodak's investment in parts – a reasonable trier of fact could find that the first was both pretextual and not the least restrictive alternative available, the second was clearly pretextual, and the third was insufficient as a matter of law. Pet. App. 12A-15A.

The Ninth Circuit also reversed the summary judgment granted against the ISOs on their claims under section 2 of the Sherman Act. Noting that a monopolist may not refuse to deal with a competitor in an exclusionary attempt to impede competition without a legitimate

[5] Under Ninth Circuit precedents, a tying arrangement "does not violate the antitrust laws 'if implemented for a legitimate business reason and if no less restrictive alternative is available.'" *Mozart Co. v. Mercedes-Benz of North America, Inc.*, 833 F.2d 1342, 1349 (9th Cir. 1987), *cert. denied*, 109 S. Ct. 179 (1988); *Phonetele, Inc. v. American Tel. & Tel. Co.*, 664 F.2d 716, 739 (9th Cir. 1981).

business justification, and that a monopolist may not deny a competitor access to an "essential facility", the Court of Appeals concluded that the ISOs' evidence, as summarized above, raised triable issues under both of these theories. Pet. App. 16A-17A. And for essentially the same reasons that it had rejected Kodak's business justifications on the tying claim, the Court also rejected them as defenses to the monopolization claims. *Id.* at 17A-18A.

Judge Wallace in his dissent conceded the ISOs had "raised triable issues as to whether Kodak's business practices constitute a tying arrangement." *Id.* at 20A. However, he agreed with Kodak's theoretical model that it could not have market power in the "derivative aftermarket for replacement parts." *Id.* at 20A-25A. With respect to the section 2 claims, he concluded that Kodak's alleged business justifications were sufficient to defeat liability.

Kodak's petition for rehearing and suggestion for rehearing *en banc* was denied on September 21, 1990, with no judge of the court requesting a vote on it.

REASONS FOR DENYING THE WRIT

Summary of Argument

In its petition for certiorari, Kodak ignores the evidence that the Ninth Circuit held sufficient to raise triable issues on the question of market power under respondents' tie-in theory and monopoly power under respondents' monopolization theory. Instead, Kodak urges the Court to substitute "perfect-world" economic theory for imperfect reality and hold *as a matter of law* that so long as a manufacturer competes in the interbrand equipment market, it cannot have sufficient economic power to impose an unlawful tie or to monopolize in any derivative "aftermarket", whether for parts, service or otherwise.

Even if such a broad ruling could ever be justified, this is plainly not the case in which to announce it. The

Ninth Circuit reversed the summary judgment below because the meager record that respondents were permitted to develop convinced the Court of Appeals that the actual "aftermarkets" in which Kodak competes had not behaved as Kodak's economic theory would suggest. Because a motion for summary judgment should be granted only after the party opposing the motion has had "an opportunity to make full discovery," *Celotex Corp. v. Catrett*, 477 U.S. 317, 326 (1986), and because that opportunity was denied here, the Court of Appeals' conclusions about the triable issues raised by Kodak's tying arrangements and monopolization should not be disturbed.

Kodak is wrong in arguing that the decision below is inconsistent with this Court's analysis of tying arrangements in *Jefferson Parish Hospital Dist. No. 2 v. Hyde*, 466 U.S. 2 (1986). In *Jefferson Parish*, the Court was careful to point out that while the market imperfections in the record before it were insufficient to create the requisite economic power in the market for hospital services, some market imperfections – such as imperfect consumer information – can cause buyers "not [to] be fully sensitive to the price or quality implications of a tying arrangement," thus "imped[ing] competition on the merits." 466 U.S. at 15, n.24. That is precisely the situation the Ninth Circuit faced here: because Kodak changed its long-standing policy and practice on parts availability, no one who purchased Kodak photocopiers or micrographic equipment before the change could have accurately estimated the increased service costs that would be brought about by Kodak's unanticipated tying behavior.

Nor is Kodak convincing when it argues that certiorari is appropriate because the decision below conflicts with decisions from other circuits, such as *Grappone v. Subaru of New England, Inc.*, 858 F.2d 792 (1st Cir. 1988) and *A.I. Root Co. v. Computer/Dynamics, Inc.*, 806 F.2d 673 (6th Cir. 1986). These cases do not lay down a general rule that interbrand competition precludes a finding of

economic power in "aftermarkets"; they simply hold that on the varying facts presented, the tie-ins at issue were lawful.

Kodak is also wrong in contending that the decision below contravenes the standards for summary judgment announced in *Matsushita Elec. Indus. Co. v. Zenith Radio*, 475 U.S. 574 (1986). As this Court held in *Celotex*, summary judgment should not be granted in any case governed by Rule 56 until the party opposing the motion has had "an opportunity to make full discovery." 477 U.S. at 326. *Matsushita* is not inconsistent with this general principle; it stands only for the proposition that where an antitrust plaintiff who has conducted full discovery alleges an "implausible" conspiracy, that plaintiff must come forward in its opposition to the motion "with more persuasive evidence to support [its] claim than would otherwise be necessary." 475 U.S. at 587. *Matsushita* does *not* hold that in all cases where economic theory suggests that an unlawful restraint on competition is unlikely to occur, discovery can be denied even in the face of evidence that is contrary to the theory. In view of the Ninth Circuit's conclusion that respondents' evidence of economic reality was contrary to Kodak's economic theory, it was not error to reverse the summary judgment and to allow discovery to proceed.

Kodak's argument that the law uniformly protects refusals by a supplier to deal with a competitor was rejected by this Court in *Aspen Skiing Co. v. Aspen Highland Skiing Corp.*, 472 U.S. 585 (1985), and by the Ninth Circuit below. Under certain facts, which the panel below found to be triable issues of fact in this case, such refusals to deal can be illegal under section 2 of the Sherman Act. These facts include (1) Kodak's prior policy and practice of supplying parts to ISO competitors, (2) Kodak's reversal of its policy in response to ISOs' competition through high-quality/low-priced service, (3) Kodak's targeting and impacting ISOs and, (4) a lack of legitimate business justifications for Kodak's actions. Review should be denied to allow respondents the opportunity for full discovery on these issues.

Kodak's attempt to avoid these facts, by relying on an abstract economic theory that interbrand competition in equipment obviates the need to worry about market power in parts or service aftermarkets, is contrary to this Court's standards in *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956) and *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962) the U.S. Department of Justice Merger Guidelines and the facts in this case.

Likewise, whether Kodak's alleged "business justifications" are the real ("legitimate") reasons for Kodak's actions, or whether they are merely "pretextual", because anticompetitive reasons predominate, cannot be reviewed without a full factual record, as existed in *Aspen Skiing* and all other cases relied upon by Kodak.

I. THE OPINION BELOW IS CONSISTENT WITH OTHER DECISIONS HOLDING THAT SUMMARY JUDGMENT SHOULD NOT BE GRANTED IN ANTITRUST CASES UNTIL THE PLAINTIFF HAS BEEN AFFORDED AN OPPORTUNITY TO CONDUCT ADEQUATE DISCOVERY

Kodak contends that resolution of the issues raised in its petition "is critical to manufacturers in high technology industries," and that without a ruling now from this Court that manufacturers in the interbrand equipment market may freely impose tying arrangements or monopolize in "aftermarkets" for their products, there will be a "chilling impact . . . on procompetitive innovation". Petition, pp. 10, 11.

One would scarcely guess from reading this apocalyptic rhetoric that the case at issue was decided not on the basis of a full trial record, but rather on summary judgment after very limited discovery. Indeed, it is not until page 22 of its petition (at footnote 8) that Kodak even hints that the record before the District Court was based upon one limited set of interrogatories, one limited

round of document production, and six depositions. *See* Pet. App. 36B-37B.

Under these circumstances, it is clear that the Ninth Circuit did not err in reversing the summary judgment granted by the District Court, because Kodak's motion for summary judgment was premature. As noted above, it was made just four months after filing of the complaint, before any discovery had been conducted. In *Celotex*, this Court pointed out that such premature motions should be

> dealt with under Rule 56(f), which allows a summary judgment motion to be denied, or the hearing on the motion to be continued, *if the non-moving party has not had an opportunity to make full discovery*.

477 U.S. at 326 (emphasis supplied). Perhaps if the District Court had followed that course of action here, it would not have misperceived the nature of the tie-in that respondents alleged. *Compare* Pet. App. 5A with 32B-33B.

The Court of Appeals' decision is not only consistent with *Celotex*, but also with a long line of other Court of Appeals decisions in which summary judgments have been reversed for allowing plaintiffs little or no discovery. *See Intern. Raw Materials v. Stauffer Chemical*, 898 F.2d 946, 949 (3d Cir. 1990) (summary judgment reversed where plaintiff denied discovery on facts concerning alleged Webb-Pomerene Act antitrust exemption); *Mannington Mills v. Congoleum Industries, Inc.*, 610 F.2d 1059, 1073-74 (3d Cir. 1979) (summary judgment on antitrust claim reversed where plaintiff had been allowed no discovery in antitrust phase of combined patent/antitrust case); *Egelston v. State University College at Geneseo*, 535 F.2d 752 (2d Cir. 1976) (summary judgment reversed where plaintiff in Title VII case had been allowed no discovery on facts concerning limitations period); *Ward v. United States*, 471 F.2d 667, 670 (3d Cir. 1973) (summary judgment reversed in Federal Tort Claims Act case where government affidavits left open the possibility of operational negligence in jet aircraft flight, and plaintiff had requested a continuance under Rule 56(f)).

Until the contours of the tie-in and monopolization alleged by respondents and the business justifications offered by Kodak have been fleshed out through further discovery, the Ninth Circuit's decision cannot be properly reviewed, nor does it provide a basis for the broad rulings that Kodak seeks.

II. THE DECISION BELOW IS NOT INCONSISTENT WITH THIS COURT'S ANALYSIS OF TYING ARRANGEMENTS IN *JEFFERSON PARISH*

The principal thrust of Kodak's attack on the decision below is its alleged inconsistency with the tests for market power in *Jefferson Parish*. Leaping upon the Ninth Circuit's common-sense observation that "market imperfections can keep economic theories about how consumers will act from mirroring reality," Pet. App. 10A, Kodak asserts that the Court of Appeals substituted "speculative inferences about unidentified market imperfections" for the careful analysis of economic power in the tying product market that *Jefferson Parish* requires to show a *per se* tying violation of section 1 of the Sherman Act, 15 U.S.C. § 1. Petition, p. 16.

Kodak's argument is without merit. It reflects a highly selective reading of *Jefferson Parish*, emphasizing that case's resolution of the specific facts before it while ignoring the case's more general, but equally important, teachings about the role of market imperfections in tying analysis. Kodak's argument also ignores the record in this case, which – limited though it was – clearly suggested to the Ninth Circuit the presence of market imperfections similar to those referenced in *Jefferson Parish*.

The Ninth Circuit's reference to market imperfections was not pulled out of thin air. It was taken from footnote 24 of *Jefferson Parish*, in which the Court elaborated on its statement about how, in an unlawful tying situation, consumers can be harmed by the foreclosure of competition in the market for the tied product. In footnote 24, the Court said:

> Especially where *market imperfections* exist, purchasers may not be fully sensitive to the price or quality implications of a tying arrangement, and hence it may impede competition on the merits. *See* Craswell, [Tying Requirements in Competitive Markets: The Consumer Protection Issues, 62 B.U.L. REV. 661,] at 675-679.

466 U.S. at 15, n.24 (emphasis supplied).

The law review article cited in footnote 24 lists a number of imperfections that may engender power in the market for the tying product, and at least two of them correspond with the facts here. The article notes that one market imperfection is:

> [D]iscovering whether or not a tie will even be imposed . . . In a number of recent cases . . . buyers have alleged that they were forced to buy the tied product . . . by the seller's threat to cut off the supply of the tying product after the initial purchases had already begun . . .
>
> . . . Obviously, there will be no harm if the buyer can switch to some other source for the tying product when the original seller begins to insist on a tie. In some cases, though, the buyer would encounter significant transaction costs in switching to another supplier . . . Conceivably, the [seller] could then introduce new tying requirements that the [buyer] would not have originally agreed to, up to the point where the cost of such requirements exceeds the cost of switching to a different [seller's] system.

Craswell, *supra*, at 674-75.

The facts before the Ninth Circuit showed that this circumstance applies to owners of Kodak machines. As the Ninth Circuit said, "some owners of large Kodak equipment packages will pay higher prices for Kodak service rather than switch to competitors' systems." Pet. App. 11A.

Another market imperfection described in the Craswell article concerns buyers who are not prescient about future costs:

> The simplest explanation for tie-ins which do not benefit buyers is that the buyer was not aware of what he was agreeing to. This may be due . . . to the difficulty in calculating in advance of the sale just how much a tie-in is likely to cost over the course of the contract . . . The important point for the moment is that so long as buyers do not *perfectly understand* the tying arrangement, they will get into some ties that they would have preferred to stay out of, and which would represent a net efficiency loss.

Craswell, *supra*, at 672 (footnote omitted; emphasis supplied).

The evidence before the Ninth Circuit showed that this circumstance also applies to owners of Kodak machines: prior to 1985, Kodak imposed no restrictions on the sale of repair parts. Pet. App. 3A. A customer who purchased a Kodak machine before that time could not have accurately estimated the costs of the tying arrangement that Kodak now imposes.

Kodak is correct in stating that in *Jefferson Parish*, the Court found the market imperfections before it insufficient (along with the defendant hospital's 30% market share) to create market power in the tying product market. However, the basis for that conclusion was *not* – as Kodak implies – that market imperfections never matter, but rather that the imperfections identified by the Fifth Circuit were irrelevant:

> Tying arrangements need only be condemned if they restrain competition on the merits by forcing purchases that would not otherwise be made. [The] lack of price or quality competition [identified by the Fifth Circuit] does not create this type of forcing. If consumers lack price consciousness, that fact will not force them to take an anesthesiologist whose services they do not want – their indifference to price will have no impact on their willingness or ability to go to another hospital where they can utilize the services of the anesthesiologist

> of their choice. Similarly, if consumers cannot evaluate the quality of anesthesiological services, it follows that they are indifferent between certified anesthesiologists even in the absence of a tying arrangement . . .

466 U.S. at 27-28.[6]

The Ninth Circuit was correct when it concluded that the market imperfections suggested by the record here *do* matter, and Kodak has presented no sound reason for disturbing that conclusion in the absence of full discovery.

In addition to arguing that the decision below is contrary to *Jefferson Parish*, Kodak asserts that the Ninth Circuit's alleged analytical flaws were "exacerbated" by the panel's reliance on the "questionable decision" in *Digidyne Corp. v. Data General Corp.*, 734 F.2d 1336 (9th Cir. 1984), *cert. denied*, 473 U.S. 908 (1985). In *Digidyne*, the Ninth Circuit held that the power in the tying product market, a copyrighted operating system, was enhanced by the huge investment customers had made to develop applications software that worked only with this operating system. Thus, these customers could not easily switch to other systems – they were "locked in" – when the manufacturer conditioned availability of its operating system, the tying product, on the customers' agreement to purchase only its brand of central processing units, the tied product. 734 F.2d at 1342-43.

Kodak is correct that the decision below is based in part on evidence showing that Kodak machine customers are also "locked-in". Kodak is also correct that panels in some circuits have criticized *Digidyne*.[7] What Kodak fails

[6] In contrast, the evidence before the Ninth Circuit in this case showed that there was substantial price and quality competition between Kodak and ISOs, and that consumers were well aware of and cared about the differences. Pet. App. 3A, 10A-11A.

[7] Other circuits, however, have applied *Digidyne*'s reasoning. *See*, e.g. *Grappone, supra*, 858 F.2d at 798.

to note, however, is that the decision in *Digidyne* was based upon the record of a trial that lasted 45 days. *Id.* at 1339. Because the District Judge cut off discovery at such an early stage in this case, the decision below is obviously not a suitable vehicle for reviewing the issues raised by *Digidyne*.

III. THE DECISION BELOW DOES NOT CONFLICT WITH DECISIONS FROM OTHER CIRCUITS CITED BY KODAK

In addition to arguing that the decision below is inconsistent with *Jefferson Parish*, Kodak asserts that the panel's opinion conflicts with several decisions from other circuits, especially *Grappone v. Subaru of New England, Inc., supra*, and *A.I. Root Co. v. Computer/Dynamics, Inc., supra*. Kodak asserts that these cases, along with the Ninth Circuit's own prior decision in *General Business Systems v. North American Philips Corp.*, 699 F.2d 965 (9th Cir. 1983), stand for the proposition that "interbrand competition necessarily precludes market power in derivative aftermarkets." Petition, p. 18.

Kodak's claim of a conflict among the circuits cannot withstand close scrutiny. It is evident that *Grappone, A.I. Root* and *General Business Systems* do not, alone or together, lay down the broad rule urged by Kodak.

Before considering these cases, it is useful to bear in mind just what the fundamental premise in Kodak's argument is. Judge Wallace's dissenting opinion below clearly recognizes it: that charging excessive prices for service will eventually harm Kodak in the supposedly more lucrative interbrand market for equipment. Pet. App. 20A-23A. This premise ignores the magnitude of service market profits and the damage that an unlawful tie or monopolization actually inflicts in the *short-run* upon competition and consumers in the service market.

Quite apart from this weakness in its theory, the cases cited by Kodak do not support its theory. In *Grappone*, for example, Subaru's New England distributor was

found to have tied the availability of Subaru cars to a Subaru dealer's purchase of parts kits in 1973 and 1974, which included some parts the dealer did not want (and many that it did). 858 F.2d at 793-94. The First Circuit reversed.

The *Grappone* court reviewed the tests for market power in *Jefferson Parish*, and concluded that the distributor met none of them. Since Subaru sold only a tiny percentage of the cars in New England, power in the tying product market (cars) could not be predicated on market share. *Id.* at 797. And since only 3 of the distributor's 64 dealers had protested the alleged over-inclusiveness of the parts kits, market power could not be shown by coercion. *Id.* at 797-98. The Court also noted that the damages plaintiff allegedly sustained by having to buy too many parts were trivial, so market power could not be inferred from any alleged ability on defendant's part to raise prices in the tied product market (parts). *Id.* at 798.

Finally, the First Circuit pointed out the substantial evidence in the record that defendant had developed the parts kit to insure that Subaru dealers would have enough parts on hand to repair the cars in the first year after sale. Given that Subaru was a relatively new entrant into the U.S. car market,

> [T]he record indicates that Subaru was a small firm attempting to break into the industry; it shows that the tie plausibly served the procompetitive purpose of helping the firm develop or maintain sales.

Id. at 799. Thus, the parts policy appeared to come within the well-recognized exception to *per se* liability for tying arrangements imposed to facilitate entry into a new market. *See United States v. Jerrold Electronics Corp.*, 187 F. Supp. 545, 556-58 (E.D. Pa. 1960), *aff'd per curiam*, 365 U.S. 567 (1961).

Grappone not only fails to support the broad rule Kodak claims, but its careful analysis of market power

underscores the correctness of the Ninth Circuit's decision here. As the Ninth Circuit pointed out, there was evidence Kodak had been able to coerce equipment customers into accepting its service, and Kodak was clearly able to exact a significantly higher price for service than did ISOs. Pet. App. 10A-11A.

Kodak's argument also finds no comfort in *A.I. Root*. In that case, a small business alleged that the defendant computer services company had sought to tie the availability of updated software for plaintiff's computer to the plaintiff's agreement to use the software only with equipment manufactured and sold by defendant.

In affirming summary judgment for the defendant, the Sixth Circuit ruled that the necessary power in the tying product market could not be found, because (1) defendant had a very small share in the computer market, and (2) the fact the software was copyrighted was not enough to make it uniquely attractive to buyers. 806 F.2d at 675-77. Moreover, the defendant had sought to impose the tie only prospectively; i.e., on plaintiff's agreement to buy defendant's hardware in the future. *Id.* at 677.

Like *Grappone*, the decision in *A.I. Root* shows the correctness of the ruling below. Unlike Kodak service customers, the plaintiff in *A.I. Root* had the option to and did switch computer brands when the defendant sought to impose a tie. *Id.* at 675. Further, since the tie in *A.I. Root* was prospective only, the plaintiff there was not in the position of Kodak customers, many of whom bought machines before Kodak began refusing to sell repair parts to ISOs for these machines.

In a final effort to support its argument on interbrand competition, Kodak argues that the decision below is inconsistent with the Ninth Circuit's own decision in *General Business Systems*. In that case, a former distributor for Philips small business computers brought suit against

Philips on a variety of antitrust theories.[8] One of these theories was that Philips had tied the availability of service and warranty protection for its computers to agreement by its customers to use only Philips-brand magnetic ledger cards ("mlcs"), an essential component for operating the computers. However, the evidence showed that Philips mlcs were superior to other brands, and that their price did not decline even after Philips abandoned the small computer market and sold its mlc business. 699 F.2d at 977. Since the power to raise prices for the tied product is one of the indicia of an illegal tie, *Fortner Enterprises, Inc. v. United States Steel Corp.*, 394 U.S. 495, 513 n.6 (1969) (White, J., dissenting), and since that had not happened with respect to the mlcs, *General Business Systems'* rejection of the plaintiff's tying claim was consistent with conventional tying analysis. Such analysis is not in conflict with the decision below, because the Ninth Circuit noted that in this case, Kodak has been able to extract higher prices for service (the tied product) than the price that prevailed where Kodak had to compete with ISOs. Pet. App. 3A.

IV. THE NINTH CIRCUIT'S DECISION IS NOT INCONSISTENT WITH THE SUMMARY JUDGMENT STANDARDS IN *MATSUSHITA*

In addition to arguing that the opinion below departed from proper tying analysis, Kodak vigorously contends that the Ninth Circuit misapplied the summary judgment standards applicable in antitrust cases. Specifically, Kodak argues that *Matsushita Elec. Indus. Co. v. Zenith Radio, supra*, imposes a heightened burden on an antitrust plaintiff resisting summary judgment, and that if the plaintiff's claim seems contrary to "economic

[8] One of these theories was monopolization. The quotations from *General Business Systems* at page 19 of Kodak's petition are from the Ninth Circuit's discussion of this issue, not the tying claim.

sense", plaintiff can defeat the motion only by coming forward with even more persuasive evidence than would otherwise be necessary. Petition, pp. 20-23.

As noted above, it was Kodak's premature motion and the District Court's failure to allow adequate discovery that are responsible for the lack of a complete factual record. Even if the record below were more fully developed, however, *Matsushita* would not support Kodak.

In *Matsushita*, this Court held, in reliance on *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), that because the plaintiff American manufacturers had alleged an inherently implausible predatory pricing conspiracy by Japanese electronics manufacturers, it was appropriate to require that the plaintiffs produce – after years of discovery – factual evidence that was more consistent with their conspiracy theory than with unilateral action. 475 U.S. at 588-98. Because the plaintiffs were unable to do so, the Court reversed the Third Circuit's decision that summary judgment had been improperly granted.

Since it was decided in 1986, *Matsushita's* requirement that an antitrust plaintiff asserting an economically "implausible" claim "must come forward with more persuasive evidence to support [its] claim than would otherwise be necessary", *id.* at 587, has been confined to conspiracy cases. P. Areeda & H. Hovenkamp, Antitrust Law ¶ 316.1b (Supp. 1990).

Respondents' tie-in and monopolization claims are entirely different from the conspiratorial predatory pricing scheme alleged in *Matsushita*. Here, the key issue is whether Kodak enjoys sufficient economic power in the parts market so that it can *unilaterally* force customers to purchase its service or put ISOs out of business. Because the Ninth Circuit panel found that respondents had presented enough evidence – even given the discovery limitations imposed upon them – to raise triable issues on these questions, its decision is not inconsistent with *Matsushita* and should not be disturbed.

V. COMPETITION IN INTERBRAND EQUIPMENT MARKETS DOES NOT, AS A MATTER OF LAW, PREVENT VIOLATION OF THE SHERMAN ACT IN AFTERMARKETS

Kodak argues that competition in the interbrand market means as a matter of law that "Kodak has no market power and no ability to act anticompetitively in any derivative parts or service aftermarket," and that this prevents it from having market power under section 1 of the Sherman Act or monopoly power under section 2 of the Sherman Act. Petition, p. 9. This argument is fundamentally flawed, as shown by the standards this Court uses to define relevant markets and market power, the Department of Justice Merger Guidelines, and the facts of this case.

A. Relevant Markets Under *du Pont* and *Brown Shoe*

The standards for defining a relevant market or submarket in which competition is measured for antitrust purposes were set forth by this Court in *United States v. E.I. du Pont de Nemours & Co., supra* and *Brown Shoe Co. v. United States, supra.*

In *du Pont* this Court said:

> [T]he relevant market depends upon the availability . . . of alternative commodities for buyers: i.e., whether there is a cross elasticity of demand. . . .

351 U.S. at 380. Cross-elasticity of demand expresses how price movement in one market affects demand for goods or services in other markets. Where the price of one product increases sharply and there is a significant shifting between products, the products are close substitutes and therefore in the same relevant market. The Ninth Circuit properly found the relevant market to be a triable issue of fact in this case, because respondents showed that although Kodak charges up to twice as much as ISOs for service, "some owners of large Kodak equipment

packages will pay higher prices for Kodak service rather than switch to competitors' systems." Pet. App. 11A.

In *Brown Shoe* this Court examined the "practical indicia" of the marketplace in order to define the relevant market. 370 U.S. at 325. These practical indicia include:

> [I]ndustry or public recognition of the submarket . . . , the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors. *Id.*

The Ninth Circuit applied these tests properly when it found facts that a reasonable trier of fact might consider sufficient to prove that an "aftermarket" can be a relevant market under the *Brown Shoe* "practical indicia" standard.

B. The Flawed Kodak Economic Theory

Kodak, *amici* and Judge Wallace's dissent in the Ninth Circuit place great reliance on the theory, set out in the dissent of Judge Posner in *Parts & Electric Motors, Inc. v. Sterling Electric, Inc.*, 866 F.2d 228 (7th Cir. 1988), *cert. denied*, 110 S.Ct. 141 (1989), that interbrand equipment competition always prevents "monopoly power" or even "market power" in a parts or service aftermarket.[9]

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[9] Although Judge Posner would substitute theory for facts, the majority in *Sterling* did not. It affirmed a jury verdict that Sterling had engaged in a *per se* tie-in by conditioning sale of its unique parts on plaintiff's purchases of motors. 866 F.2d at 232-34. Plaintiffs in *Sterling* were prospective "buyers" of new motors who had alternative suppliers, not like "owners" of Kodak equipment needing parts and service who do not have alternative suppliers. *See Dimidowich v. Bell & Howell*, 803 F.2d 1473, 1480 n.3 (9th Cir. 1986), *modified*, 810 F.2d 1517 (1987) ("[A]n owner of broken Bell & Howell micrographic equipment is indifferent to people who can service Kodak or 3M machines. If the owner's only option is to request service from Bell & Howell [or an ISO] . . . that is obviously the market he faces").

This theory does not match reality. Kodak admits the reality is that "Kodak can charge supercompetitive prices" in the service market. Petition, p. 22.

In order to try to save its theoretical economic argument, Kodak is then forced to argue, without any factual basis in the record, that charging supercompetitive prices for service could only be done in the "short run", because such a policy would be "suicidal" in the interbrand equipment market. From this, Kodak then concludes, as Judge Posner did, that this would only result in a "brief perturbation in competitive conditions [which] is not the sort of thing the antitrust laws do or should worry about." Petition, p. 8.

Not only does Kodak fail to support factually its theory that interbrand competition would keep tie-ins or monopolization in aftermarkets "small" and "short-lived," but the U.S. Department of Justice Merger Guidelines and the facts before the Ninth Circuit suggest exactly the opposite. In the Guidelines the Department of Justice has determined that market power may exist if a competitor can raise prices by a significant amount over the competitive level (generally *five percent*) for a significant time (generally *one year*).[10] The record here shows that Kodak was able to exact a price for service *one hundred percent* over competitive levels *for several years* before ISOs came into the picture (as well as after ISOs appeared, because of the Kodak actions challenged here). Pet. App. 3A. With the large service market for Kodak machines and the high cost of Kodak service, the "brief perturbation" caused by Kodak's practices in this case has, and likely will, cost consumers of Kodak service hundreds of millions of dollars in anticompetitive exactions if it continues. This is something the antitrust laws do, and should, "worry about." The markets for Kodak parts and service are relevant markets and the evidence below suggests that Kodak has unlawfully exercised market and monopoly power in them.

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[10] U.S. Department of Justice Merger Guidelines, June 14, 1984, Section 2.11.

VI. TRIABLE FACTUAL ISSUES WERE RAISED WHETHER KODAK UNLAWFULLY MAINTAINED MONOPOLY POWER IN SERVICE FOR KODAK MACHINES IN VIOLATION OF SECTION 2 OF THE SHERMAN ACT

Section 2 of the Sherman Act prohibits the creation or the maintenance of a monopoly through unlawful means. It prohibits "exclusionary", "anticompetitive" or "predatory" conduct by a monopolist. This Court defined such conduct in *Aspen Skiing Co. v. Aspen Highland Skiing Corp.* 472 U.S. 585 (1985) as:

> [B]ehavior that not only (1) tends to impair the opportunities of rivals, but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way."

Id. at 605 n.32 (quoting 3 P. Areeda & D. Turner, Antitrust Law, ¶ 626b at 78 (1978)).

In *Aspen Skiing*, this Court held that a monopolist may not unilaterally refuse to deal in order to discontinue long-standing policies which are important to the character of a market, if the refusal is a deliberate effort to discourage customers from doing business with its smaller competitors. 472 U.S. at 610. Such "an important change in the character of the market", *id.*, by a monopolist is subject to close scrutiny under the antitrust laws because:

> [I]n any business, patterns of distribution develop over time; these may reasonably be thought to be more efficient than alternative patterns of distribution that do not develop. The patterns that do develop and persist we may call the optimal patterns. By disturbing optimal distribution patterns one rival can impose costs upon another, that is, force the other to accept higher costs.

Id. at 604, n.31.

Using the close scrutiny described above, this Court in *Aspen Skiing* upheld the jury's determination that the

defendant's withdrawal of cooperation for joint lift tickets was for the purpose of harming its smaller competitor, not for the defendant's alleged business reasons. *Id.* at 608. The Court said:

> Thus the evidence supports an inference that [defendant] was not motivated by efficiency concerns and that it was willing to sacrifice short run benefits and consumer goodwill in exchange for a perceived long-run impact on its smaller rival.

Id. at 610-611.

Kodak's reliance on *Olympia Equip. Leasing Co. v. Western Union Telegraph*, 797 F.2d 370 (7th Cir. 1986) is therefore misplaced. Petition, pp. 27, 29. *Olympia* involved a monopolist's undisputed efforts to relinquish its monopoly in the relevant market. This was found to be a legitimate justification for its discontinuance of prior policies. 797 F.2d at 378. The facts in *Olympia* are in striking contrast to the evidence of Kodak's behavior, which was intended to allow Kodak to completely monopolize the Kodak service market, not to relinquish Kodak's participation in that market.

Moveover, the *Olympia* opinion expressly distinguished its facts from cases like the present one in which the monopolist's acts injure a competitor who is also a customer. *Olympia* explained:

> The monopoly supplier who retaliates against customers who have the temerity to compete with him, by cutting such customers off, is severing a collateral relationship in order to discourage competition. *Id.* at 376.[11]

[11] *See also, Otter Tail Power Co. v. United States*, 410 U.S. 366, 378 (1973) (use of monopoly power "to destroy threatened competition" violates § 2); *Lorain Journal Co. v. United States*, 342 U.S. 143, 155 (1951) (right to refuse to deal does not extend to situations where defendant acts with intent to create or maintain a monopoly); *Oahu Gas Service, Inc. v. Pacific*

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The facts before the Ninth Circuit, although not as fully developed as the trial record in *Aspen Skiing*, would allow a reasonable trier of fact to conclude that, as in *Aspen Skiing*: (1) Kodak had "discontinued a long standing policy" and had changed an established "pattern of distribution" with regard to the sale of parts to ISOs; (2) Kodak had directly targeted and impacted its smaller ISO rivals; and (3) Kodak was "not motivated by efficiency concerns".

Obviously, the question of what constitutes an unlawful refusal to deal is a factual inquiry. As the panel below found, the District Court's premature cut-off of discovery prevented a full factual inquiry into the relevant market and market power.

VII. TRIABLE FACTUAL ISSUES WERE RAISED WHETHER KODAK'S ALLEGED BUSINESS JUSTIFICATIONS WERE PRETEXTUAL AND NOT LEGITIMATE

Whether anticompetitive conduct violates section one[12] or section two[13] of the Sherman Act also depends

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Resources, Inc., 838 F.2d 360, 368 (9th Cir.), *cert denied*, 488 U.S. 870 (1988) (antitrust laws impose "affirmative duties" on monopolists to aid competitors under certain circumstances).

[12] In a section 1 tying case, the burden of proof is on the defendant with regard to business justifications. See note 5, *supra*.

[13] In a section 2 violation, the burden of proof is on the plaintiff to show that defendant's actions were not predominantly motivated by legitimate business purposes. *Aspen Skiing*, 472 U.S. at 604-612; *Calculators Hawaii, Inc. v. Brandt, Inc.*, 724 F.2d 1332, 1339 (9th Cir. 1983) (plaintiff must show defendant's acts "were predatory and not *predominantly* motivated by legitimate business purposes") (emphasis supplied); *Lektro Vend Corp. v. Vendo Co.*, 660 F.2d 255, 273 n.20 (7th Cir. 1981) *cert. denied*, 455 U.S. 921 (1982).

on whether the "business justification" offered by the monopolist is "legitimate". Under *Aspen Skiing*, this is obviously a factual inquiry. 472 U.S. at 604.

In *Aspen Skiing*, this Court applied a "predominance" standard to evaluate the "legitimacy" or "validity" of the "justifications" offered by defendant. The Court reasoned:

> Ski Co. did not persuade the jury that its conduct was justified by any normal business purpose . . . The jury may well have concluded that Ski Co. elected to forego these short-run [business] benefits because it was *more interested* in reducing competition in the Aspen market over the long run by harming its smaller competitor.

Id. at 608. (Emphasis supplied.)

Respondents presented the same type of evidence below from which a jury could find under *Aspen Skiing* standards, that Kodak's alleged business "justifications" were invalid, including: (1) a prior course of unrestricted business dealings with competitor ISOs; (2) a change of policy by Kodak that was "an important change in the character of the market," (3) a substantial impact on competitor ISOs; and (4) a substantial impact on the relevant consumers, Kodak equipment owners. *Id.* at 605.[14]

In *Aspen Skiing*, defendant Ski Co. offered a "justification" like Kodak's first "justification", to wit, a "desire to disassociate itself from . . . inferior [skiing] services." *Id.* at 609-610. This was rejected by the *Aspen Skiing* Court,

[14] *Aspen Skiing* additionally set out types of anticompetitive evidence, also presented by respondents in this case, that can refute a monopolist's proffered business justifications, including: (1) statements made by officers or agents of the company, (2) evidence that the conduct was used threateningly and did not continue when a rival capitulated, and (3) evidence that the conduct was not related to any efficiency. *Id.* at 608 n.39.

because preserving the consumers' opportunity to choose between competitors "allowed consumers to make their own choice on these matters of quality." *Id.* at 610. Respondents also presented substantial evidence directly refuting Kodak's claim of higher quality Kodak service. Pet. App. 3A, 10A.

Kodak's second "justification" – reduction of Kodak's inventory costs – was found by the panel below to be clearly pretextual. Kodak has not rebutted respondents' logic, adopted by the Ninth Circuit, that "equipment owners' need for Kodak-supplied parts is determined only by the frequency of [Kodak] equipment failure," Pet. App. 14A. Kodak's alleged "justification" here simply makes no economic sense. Kodak must inventory parts based on the Kodak machine population and its frequency of failure. Kodak may even inventory more parts if it services all Kodak machines rather than shares service with ISOs, since ISOs inventory some Kodak parts themselves.

Kodak's third "justification", to prevent alleged "free riders" from buying parts from Kodak and then competing with Kodak for service, was found by the Ninth Circuit to be an insufficient justification "as a matter of law." Pet. App. 14A. Moreover, it is wholly disingenuous, because the record below showed that Kodak makes high profits from the sale of its parts to ISOs.

Every case relied upon by Kodak to support the "legitimate business justification" defense involved a complete factual record upon which to evaluate the "predominance" of proffered business justifications or predatory conduct.[15] Such a record does not exist in this case.

[15] *Mozart Co. v. Mercedes-Benz of North America, Inc., supra* (substantial evidence at trial supported jury finding of predominance of defendants' business justification); *Calculators Hawaii, Inc. v. Brandt, supra* (plaintiff failed to proffer *any* evidence of anticompetitive intent at trial); *Oahu Gas Service,*

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There are clearly triable issues of fact as to whether Kodak's actions "were predatory and not predominantly motivated by legitimate business purposes."

CONCLUSION

Kodak's petition for a writ of certiorari should be denied.

Respectfully submitted,

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Inc. v. Pacific Resources, Inc., supra (defendant proved clearly at trial a predominant economic justification); *Ocean State Physicians Health Plan, Inc. v. Blue Cross & Blue Shield of R.I.*, 883 F. 2d 1101 (1st Cir. 1989), *cert. denied*, 110 S. Ct. 473 (1990) (judgment NOV after jury trial that obtaining lowest prices for consumers was valid business justification); *Drinkwine v. Federated Publications, Inc.*, 780 F.2d 735, (9th Cir.), *cert. denied*, 475 U.S. 1087 (1986) (directed verdict after jury trial because plaintiff had failed to produce sufficient evidence of liability and defendant's business justifications were found to be valid).

Kodak's cite to *Bell v. Dow Chem. Co.*, 847 F.2d 1179 (5th Cir. 1988) is misleading since the Fifth Circuit found as to the business justification that " . . . significant evidence [by plaintiff] undercutting the credibility of the justifications by Dow," created inconsistences which "raise an issue of fact as to whether Dow had a justified purpose", and that this "should be left to a jury." *Id.* at 1186.